

# Interactive Brokers Quarterly Order Routing Report

## Quarter Ending September 30, 2013

### **I. Introduction**

Interactive Brokers (“IB”) has prepared this report pursuant to a U.S. Securities and Exchange Commission (“SEC”) rule requiring all brokerage firms to make publicly available quarterly reports describing their order routing practices. This report is intended to describe how and where customer orders are routed when customers use IB’s Smart Order Routing System rather than directing their order to a particular market center.

### **II. IB’s Order Routing System**

Interactive Brokers offers its customers two primary methods of routing their orders to the market for execution. First, IB customers may directly route their orders to a particular market of their choice. For stocks and options traded at exchanges or ECNs, however, IB recommends that customers use IB’s intelligent Best Execution Order Routing System (“Smart Routing<sup>SM</sup>”), which is designed to optimize both speed and total cost of execution. IB’s Smart Routing system continually scans competing market centers and automatically seeks to route orders to the best market, taking into account factors such as quote size, quote price, liquidity-taker costs, liquidity-provider rebates and the availability of automatic order execution.

**Automatic Execution and Price Improvement:** Electronic Communication Networks (“ECNs”) and exchange automatic execution systems generally execute orders instantaneously at the posted bid or offer, rather than routing orders to a specialist or a trading crowd for manual handling. Generally, when an IB customer selects Smart Routing, IB routes eligible customer orders to exchanges and market centers currently offering automatic execution of orders. While automatically executed orders may not have an opportunity to be executed at a price better than the market center’s posted bid or offer, automatic execution of customer orders is faster and more certain than other methods of execution and eliminates execution of orders at prices inferior to the prices posted when the order was routed to the market. Automatic execution of orders also eliminates the ability of a market maker or a specialist to hold a customer order and perhaps decline to execute the order if the market moves in the customer’s favor while the order is pending. Overall, IB believes that use of the Smart Routing system to route orders to the exchange or market center with the best price, combined with automatic execution, provides IB customers with the most favorable order execution.

**IB’s Order Routing System and Reg NMS:** For U.S. stocks, IB’s Smart Routing system is designed to comply fully with Regulation NMS and with our duty as a broker-dealer to provide best execution for customer orders. IB’s Smart Routing system connects to all Regulation NMS exchanges and public market centers and IB receives direct market data feeds from these market centers. Therefore IB can route an order directly to the market with the best price. If an order is not executed immediately, IB’s system then constantly monitors the open order and in most cases will cancel and reroute it if market conditions or prices change and another market center becomes more favorable for the order. If an order is too large to be executed at the best price at a single exchange or market center, IB’s Smart Routing system will split the order and send it to multiple destinations to get the fastest fill at the most favorable price.

**Intermarket Sweep Orders for U.S. National Market System Stocks:** Because IB’s system monitors the available markets and is designed to send orders only to the markets posting the best price, orders routed by the IB Smart Routing system generally will be marked as “Intermarket Sweep Orders” – “ISOs” – meaning that an exchange that receives such an order will be able to execute the

order in reliance that the IB system did not identify any better prices for the order, or that other orders sent at or around the same time by IB have already taken out any better priced quotes on other exchanges or market centers. IB has certain processes in place to monitor its connections to various exchanges and market centers, the quality of its market data feeds, and the quality of its order executions. If an exchange system or the IB system is experiencing technical problems or if IB is not connected to the market that is posting the best price, IB may route an order to an exchange without marking the order as ISO. This will allow the receiving market to re-route the order to a market offering a better price, if necessary.

**Orders Sent Near the Opening of Trading:** Please note that markets can be especially volatile near the opening of a trading session, with prices and available volume often changing rapidly and with data feeds from various markets potentially being slow or temporarily unavailable. IB cannot guarantee that orders sent near the opening of trading necessarily will receive the best posted price. You may want to consider the use of limit orders at the open, although market orders should be used if you want a higher certainty of getting a fill.

**Order Conversion and Designation:** Interactive Brokers may convert certain order types or apply conditions to certain IB customer orders sent to IB via Smart Routing in order to facilitate an execution. For example, order types not offered by certain exchanges may be simulated by the IB system using order designations. In addition, orders may be sent Immediate or Cancel, Fill-Or-Kill, All-Or-None, etc. in order to facilitate an immediate automatic execution, consistent with the objectives of the customer order (also, see discussion of “ISO” designation above). To protect customer orders from significant and rapidly changing prices, IB generally simulates market orders on exchanges by establishing an execution cap at a percentage beyond the inside bid/ask. While this cap is set at a level intended to balance the objectives of execution certainty and minimized price risk, there exists a remote possibility that an execution will be delayed or may not take place. In addition, certain exchanges, as a protective measure, impose their own price caps or bands upon market orders at levels that can be more or less restrictive than those imposed by IB, and which may similarly affect the speed and certainty of order execution.

**Payment for Order Flow – Stocks:** IB receives payments for several types of order executions in US stocks. Interactive Brokers is connected to Automated Trading Centers and also to both Electronic Communication Networks (ECNs) and Alternative Trading Systems (ATSS). Non-directed orders submitted through IB SmartRouting<sup>SM</sup> are routed to the market with the best firm prices available at the time of order routing for immediate execution, with the preference of routing orders to electronic exchanges. IB’s SmartRouting system is designed to provide IB customers with the best available order execution.

IB has relationships with certain liquidity providers to which it routes orders, in which IB receives payment for order flow in exchange for routing marketable orders to these market centers. The Smart Routing system is designed to route to these venues only when they match or exceed the best available prices in the market at that time. Currently, payment is received only for U.S. securities and only from certain market centers. For certain other venues, IB does not receive a payment but is not charged a fee for order execution. Registered exchanges and ECNs generally publish their liquidity rebate fee structures on their websites. This information is also published on IB’s website. In addition, several types of payments received by IB for various types of order executions may be considered indirect payment for order flow under SEC interpretations.

Dark Pools: IB receives order flow payments from some “dark pool” ATSS for routing orders to those dark pools. While IB benefits from these payments, IB customers also benefit from IB’s access to the dark pools. Dark pools provide a source of substantial additional liquidity. Dark pools charge

lower execution fees than exchanges. Dark pools also provide fast executions and the possibility of executions at prices more favorable than the prevailing NBBO.

ECN Rebates: IB receives liquidity rebates from ECNs for certain orders routed to those ECNs. ECN liquidity rebates are credited against the fees charged by the ECNs to execute other orders. ECN rebate amounts change frequently. Rebate rates for most ECNs are posted on the IB website in the section on Cost-Plus commission costs. These rates are also typically posted on ECN websites.

Liquidity Provider Relationships: IB has entered arrangements with certain institutions under which such institutions may send orders to IB on a “not held” basis. These orders are held within the IB system and are not displayed in the national market. If another IB customer order can be immediately executed against such an order held in the IB system (at the national best bid or offer), the orders may be crossed and the execution reported to the tape. This arrangement provides extra liquidity for some IB customer orders and leads to faster executions at the NBBO (since the orders do not have to be sent to an exchange or ECN to be executed but can be executed within the IB system). IB may receive payment in the form of commissions or otherwise from the liquidity providers for these executions.

**Payment for Order Flow – Options:** IB receives order flow payments in varying amounts from U.S. option exchanges, specialists and/or market makers pursuant to the mandatory marketing fee programs that have been adopted by the exchanges and approved by the SEC. If multiple exchanges are quoting at the NBBO for an option order and IB has discretion as to where to send the order or a portion of it, IB generally will “break the tie” by sending the order to an exchange where it will receive the most payment for the order or to an exchange designated by the firm from whom IB will receive the most payment.

Several option exchanges have adopted a “maker-taker” market structure, in which exchange members are charged for orders that take liquidity from the exchange (i.e., marketable orders that trade against a posted quote or limit order) and receive a rebate for orders that provide liquidity to the exchange (i.e., non-marketable limit orders that are posted and then trade against incoming marketable orders). The charges imposed or rebates offered by these exchanges affect the total cost of execution and IB’s Smart Routing System may take this into account in determining where and how to route option orders.

Routing to a Market that Matches NBBO to Reduce or Avoid Exchange Fees: Under certain circumstances, IB may route a marketable option order to an exchange that is not currently posting the NBBO but which may be willing to “step up” and execute the order at the NBBO. Generally, IB will do this in order to avoid or reduce the applicable fee for executing the order, compared to routing to a different exchange. IB generally will share some portion of the economic benefit of routing orders in this manner with customers in the form of reduced execution fees, although IB is not required to and does not guarantee that it will share such benefit. In addition, in the limited circumstances where IB routes orders in this manner, IB generally guarantees a fill at the NBBO at the time the order was routed.

Routing to an Option Market Where an Affiliate is Active: Interactive Brokers may route an option order to an option exchange where its affiliate Timber Hill LLC is more likely to trade with the order. In cases where the customer is eligible for a rebate for the order under IB's cost-plus commission schedule, if routing to an exchange where Timber Hill is active would reduce the rebate to be paid to the customer (or increase a fee paid by the customer) compared to a different exchange, IB generally will adjust the rebate paid to the customer (or the fee paid by the customer) to match the higher rebate (or lower fee), although IB is not required to do this and does not guarantee it.

**Option Exchange Linkage:** Under the Decentralized Linkage plan for options, markets have transitioned from the OCC linkage hub to direct order routing. The Decentralized Linkage plan is designed to address issues including locked/crossed markets, trade-throughs and Intermarket Sweep Orders (ISO) for options. Decentralized Linkage participants include Boston Options Exchange, Inc. (BOX); The Chicago Board Options Exchange (CBOE); The International Securities Exchange (ISE); NASDAQ Options Market (NSDQ); NASDAQ OMX PHLX (PHLX); NYSE Arca; NYSE Amex Options; and Miami International Securities Exchange (MIAX).

**Affiliate Relationships:** IB's affiliate Timber Hill LLC makes markets in stocks and acts as a specialist or market maker on all U.S. option exchanges. Other IB affiliates worldwide, including Timber Hill Europe, also act as market makers on global exchanges. IB's market-making affiliates may provide automatic execution for certain eligible IB customer orders routed through IB's SmartRouting system for certain securities. Orders sent to IB affiliates for automatic execution may be eligible for price improvement (i.e., they may be executed at a price better than the best posted bid or offer). As specialist on various option exchanges, IB's affiliate Timber Hill LLC may be responsible for allocating payment for order flow that is generated in its assigned option classes, depending on the design of the applicable exchange's SEC-approved payment for order flow plan. Consistent with these plans, Timber Hill pays such funds to Interactive Brokers.

**III. Order Routing Information for Particular Types of Securities**

This section provides statistical and other information about orders that are sent through IB's Smart Routing systems for the following types of securities: New York Stock Exchange ("NYSE") listed stocks; Nasdaq stocks; Stocks listed on NYSE MKT (formerly "NYSE Amex") or regional exchanges; and Exchange-listed options. For each of these types of securities, this section identifies the market centers most often selected by IB's Smart Routing systems and the percentage of various types of orders sent to those market centers. This section also addresses material relationships of IB and its affiliates to each market center to which IB routes orders.

**A. NYSE Stocks**

Summary Statistics:

Percentage of total orders that were non-directed (i.e., sent using Smart Routing).....	96.0%
Percentage of total non-directed orders that were market orders....	6.7%
Percentage of total non-directed orders that were limit orders.....	64.8%
Percentage of total non-directed orders that were other orders.....	28.5%

Market Centers Receiving Significant Percentage of Non-Directed Orders

1.	NYSE:		
		Percentage of total non-directed orders.....	53.3%
		Percentage of non-directed market orders....	20.7%
		Percentage of non-directed limit orders.....	48.4%
		Percentage of non-directed other orders.....	72.1%
2.	NYSE ARCA:		
		Percentage of total non-directed orders.....	14.0%
		Percentage of non-directed market orders....	1.4%
		Percentage of non-directed limit orders.....	18.4%
		Percentage of non-directed other orders.....	7.0%

3.	BATS Exchange:		
		Percentage of total non-directed orders.....	9.2%
		Percentage of non-directed market orders.....	2.8%
		Percentage of non-directed limit orders.....	12.0%
		Percentage of non-directed other orders.....	4.4%
4.	IBKR ATS:		
		Percentage of total non-directed orders.....	6.5%
		Percentage of non-directed market orders.....	33.3%
		Percentage of non-directed limit orders.....	5.4%
		Percentage of non-directed other orders.....	2.6%
5.	NASDAQ:		
		Percentage of total non-directed orders.....	5.6%
		Percentage of non-directed market orders.....	2.1%
		Percentage of non-directed limit orders.....	7.5%
		Percentage of non-directed other orders.....	2.3%
6.	NSX:		
		Percentage of total non-directed orders.....	2.4%
		Percentage of non-directed market orders.....	0.2%
		Percentage of non-directed limit orders.....	0.6%
		Percentage of non-directed other orders.....	7.1%

Material Aspects of IB Relationship with Execution Venues for NYSE Stocks

As described more fully above, Interactive Brokers receives direct payment for order flow from certain market centers for marketable orders in NYSE stocks. In addition, ECN liquidity rebates and commissions/fees paid to IB by liquidity providers that send *not held* orders to IB may be considered indirect payment for order flow. IB operates an alternative trading system (ATS) in accordance with the requirements under Regulation ATS, where it executes trades internally on its own platform (not on an exchange or other market) among multiple customers and liquidity providers. An affiliate of Interactive Brokers LLC (IB Exchange Corp.) owns minority interests in ISE Stock Exchange and CBOE Stock Exchange.

**B. Nasdaq Stocks**

Summary Statistics:

Percentage of total orders that were non-directed ( <i>i.e.</i> , sent using Smart Routing).....	94.9%
Percentage of total non-directed orders that were market orders....	6.7%
Percentage of total non-directed orders that were limit orders.....	68.7%
Percentage of total non-directed orders that were other orders.....	24.6%

## Market Centers Receiving Significant Percentage of Non-Directed Orders

1.	NASDAQ:		
		Percentage of total non-directed orders.....	64.8%
		Percentage of non-directed market orders.....	16.0%
		Percentage of non-directed limit orders.....	62.7%
		Percentage of non-directed other orders.....	84.1%
2.	BATS Exchange:		
		Percentage of total non-directed orders.....	11.1%
		Percentage of non-directed market orders.....	7.4%
		Percentage of non-directed limit orders.....	14.2%
		Percentage of non-directed other orders.....	3.6%
3.	NYSE ARCA:		
		Percentage of total non-directed orders.....	7.4%
		Percentage of non-directed market orders.....	3.1%
		Percentage of non-directed limit orders.....	9.8%
		Percentage of non-directed other orders.....	1.7%
4.	IBKR ATS:		
		Percentage of total non-directed orders.....	6.5%
		Percentage of non-directed market orders.....	32.9%
		Percentage of non-directed limit orders.....	4.9%
		Percentage of non-directed other orders.....	3.7%
5.	CSFBCROSS:		
		Percentage of total non-directed orders.....	3.0%
		Percentage of non-directed market orders.....	12.7%
		Percentage of non-directed limit orders.....	2.2%
		Percentage of non-directed other orders.....	2.5%

## Material Aspects of IB Relationship with Execution Venues for Nasdaq Stocks

As described more fully above, Interactive Brokers receives direct payment for order flow from certain market centers for marketable orders in Nasdaq stocks. In addition, ECN liquidity rebates and commissions/fees paid to IB by liquidity providers that send *not held* orders to IB may be considered indirect payment for order flow. IB operates an alternative trading system (ATS) in accordance with the requirements under Regulation ATS, where it executes trades internally on its own platform (not on an exchange or other market) among multiple customers and liquidity providers. An affiliate of Interactive Brokers LLC (IB Exchange Corp.) owns minority interests in ISE Stock Exchange and CBOE Stock Exchange.

### C. NYSE MKT and Regional Exchange-Listed Stocks

#### Summary Statistics:

Percentage of total orders that were non-directed (i.e., sent using Smart Routing).....	98.0%
Percentage of total non-directed orders that were market orders....	3.5%
Percentage of total non-directed orders that were limit orders.....	83.1%
Percentage of total non-directed orders that were other orders.....	13.3%

#### Market Centers Receiving Significant Percentage of Non-Directed Orders

1.	NYSE ARCA:		
		Percentage of total non-directed orders.....	39.0%
		Percentage of non-directed market orders.....	9.8%
		Percentage of non-directed limit orders.....	40.6%
		Percentage of non-directed other orders.....	36.8%
2.	NYSE:		
		Percentage of total non-directed orders.....	32.1%
		Percentage of non-directed market orders.....	2.3%
		Percentage of non-directed limit orders.....	33.1%
		Percentage of non-directed other orders.....	34.1%
3.	BATS Exchange:		
		Percentage of total non-directed orders.....	7.9%
		Percentage of non-directed market orders.....	8.2%
		Percentage of non-directed limit orders.....	8.1%
		Percentage of non-directed other orders.....	6.4%
4.	NASDAQ:		
		Percentage of total non-directed orders.....	6.8%
		Percentage of non-directed market orders.....	2.1%
		Percentage of non-directed limit orders.....	7.7%
		Percentage of non-directed other orders.....	2.0%
5.	NYSE MKT:		
		Percentage of total non-directed orders.....	4.5%
		Percentage of non-directed market orders.....	0.7%
		Percentage of non-directed limit orders.....	3.6%
		Percentage of non-directed other orders.....	10.7%

#### Material Aspects of IB Relationship with Execution Venues for NYSE MKT and Other Regional Exchange-Listed Stocks

As described more fully above, Interactive Brokers receives direct payment for order flow from certain market centers for marketable orders in NYSE MKT (formerly NYSE Amex) stocks. In addition, ECN liquidity rebates and commissions/fees paid to IB by liquidity providers that send *not held* orders to IB may be considered indirect payment for order flow. IB operates an alternative trading system (ATS) in accordance with the requirements under Regulation ATS, where it executes trades internally on its own platform (not on an exchange or other market) among multiple customers and liquidity providers. An affiliate of Interactive Brokers LLC (IB Exchange Corp.) owns minority interests in ISE Stock Exchange and CBOE Stock Exchange.

## D. Exchange-Listed Options

### Summary Statistics:

Percentage of total orders that were non-directed (i.e., sent using Smart Routing).....	99.3%
Percentage of total non-directed orders that were market orders....	3.7%
Percentage of total non-directed orders that were limit orders.....	95.1%
Percentage of total non-directed orders that were other orders.....	1.2%

### Market Centers Receiving Significant Percentage of Non-Directed Orders

1.	NYSE ARCA:	
	Percentage of total non-directed orders.....	27.4%
	Percentage of non-directed market orders....	9.4%
	Percentage of non-directed limit orders.....	28.3%
	Percentage of non-directed other orders.....	15.1%
2.	The NASDAQ Options Market (“NOM”):	
	Percentage of total non-directed orders.....	23.1%
	Percentage of non-directed market orders....	3.1%
	Percentage of non-directed limit orders.....	24.0%
	Percentage of non-directed other orders.....	10.0%
3.	BATS Exchange:	
	Percentage of total non-directed orders.....	10.3%
	Percentage of non-directed market orders....	5.3%
	Percentage of non-directed limit orders.....	10.6%
	Percentage of non-directed other orders.....	7.5%
4.	Chicago Board Options Exchange (“CBOE”):	
	Percentage of total non-directed orders.....	7.3%
	Percentage of non-directed market orders....	10.9%
	Percentage of non-directed limit orders.....	7.2%
	Percentage of non-directed other orders.....	11.6%
5.	Miami Options Exchange (“MIAX”):	
	Percentage of total non-directed orders.....	6.3%
	Percentage of non-directed market orders....	7.2%
	Percentage of non-directed limit orders.....	6.2%
	Percentage of non-directed other orders.....	6.1%
6.	Nasdaq OMX PHLX (“PHLX”):	
	Percentage of total non-directed orders.....	6.0%
	Percentage of non-directed market orders....	20.9%
	Percentage of non-directed limit orders.....	5.2%
	Percentage of non-directed other orders.....	16.8%

7.	NYSE AMEX Options:		
	Percentage of total non-directed orders.....	5.7%	
	Percentage of non-directed market orders.....	10.6%	
	Percentage of non-directed limit orders.....	5.5%	
	Percentage of non-directed other orders.....	7.6%	
8.	ISE Gemini Exchange:		
	Percentage of total non-directed orders.....	4.9%	
	Percentage of non-directed market orders.....	2.3%	
	Percentage of non-directed limit orders.....	5.0%	
	Percentage of non-directed other orders.....	4.6%	

Material Aspects of IB Relationship with Listed Option Market Centers

**Equity Investment in Boston Options Exchange Group LLC:** An affiliate of IB under common control with IB has a substantial, minority investment in the Boston Options Exchange Group LLC, which operates the Boston Options Exchange.

**Payment for Order Flow:** IB receives order flow payments in varying amounts from U.S. option exchanges, specialists and/or market makers pursuant to the mandatory marketing fee programs that have been adopted by the exchanges and approved by the SEC. If multiple exchanges are quoting at the NBBO for an option order and IB has discretion as to where to send the order or a portion of it, IB generally will “break the tie” by sending the order to an exchange where it will receive the most payment for the order, or to an exchange designated by the firm from whom IB will receive the most payment at the market.

Several option exchanges, including BOX and NYSE ARCA have adopted a “maker-taker” market structure, in which exchange members are charged for orders that take liquidity from the exchange (*i.e.*, marketable orders that trade against a posted quote or limit order) and receive a rebate for orders that provide liquidity to the exchange (*i.e.*, non-marketable limit orders that are posted and then trade against incoming marketable orders). The charges imposed or rebates offered by these exchanges affect the total cost of execution and IB’s Smart Routing System may take this into account in determining where and how to route option orders. For example, for certain types of orders and when certain exchanges are posting the best price, IB may route to a certain exchange and rely on the option intermarket linkage to get an execution at the NBBO at the lowest total execution cost (but only for those orders that have a high likelihood of being filled at the NBBO after linkage).

**Affiliate Relationships:** As specialist on various option exchanges, IB’s affiliate Timber Hill LLC may be responsible for allocating payment for order flow that is generated in its assigned option classes, depending on the design of the applicable exchange’s SEC-approved payment for order flow plan. As much as consistent with these plans, Timber Hill pays such funds to Interactive Brokers.

**IV. Order Routing Information for Particular Orders**

In addition to the basic quarterly reports, under Rule 606 of SEC Regulation NMS, a broker-dealer is required upon customer request to provide information regarding the identity of the market center to which the customer’s orders were routed for execution in the six months prior to the request, whether the order was a directed or non-directed order, and the time of the transaction, if any, that resulted from

such order. Please contact the IB Customer Service Desk in writing through the IB website at [interactivebrokers.com](http://interactivebrokers.com) if you wish to receive the foregoing routing information for any order(s) that you submitted within the past six months. Please type “Request for Order Routing Information” in the subject line of your request and please include your name, user id and account number as well as the date of the order(s), the security, the quantity, and any other information necessary to identify the order(s) (e.g., the time of day if there were several similar orders that day).